Estimates of the RRS's financial status mainly reflect the brightness or gloominess of the economic assumptions underlying projections of railroad employment. At this time, most economic assumptions (including CBO's) foresee future growth in the real Gross National Product (GNP) and declining rates of inflation. Differences among economic scenarios generally center about the assumed rate at which the economy will improve. For example, a three-year forecast constructed by Data Resources, Inc. (DRI) portrays a smaller annual growth in real GNP and a continuation of higher levels of interest rates than those currently assumed by CBO. Any set of economic assumptions, and thus estimates based on those assumptions, become more uncertain as the period of projection extends further into the future. With this caveat, the results and sensitivity of the CBO projections are discussed below and summarized in Table 4.

The CBO's estimate is based on an assuption that real GNP will grow at an average rate of 3.6 percent per year between 1982 and 1985 and 3.0 percent between 1986 and 1990. A lower growth rate would have a noticeable impact on railroad employment estimates but should not jeopardize RRS solvency so long as the nation's production of goods and services grows faster than the annual increase in prices. This conclusion is supported by comparing the RRS under CBO's and less optimistic economic assumptions.

Railroad employment, under the CBO economic assumptions, would decline gradually from a calendar year 1982 level of 495,000 to about 480,000 by the end of this decade. Because of higher RRS tax revenues and lower benefits, however, reserves for the program would increase by $526 million between 1982 and 1987 and accumulate to more than $3 billion by 1990. Annual projections consistent with the DRI economic forecast would assume an annual growth rate averaging 2.4 percent between 1982 and 1985--about 1.2 percentage points less than that projected by CBO. As a result of the smaller assumed rate of growth, estimated railroad employment for calendar year 1984 would fall by 16,000, or 3.2 percent. This suggests that in order for railroad employment to fall below 450,000 in 1984, the nation's economy could not expand (no real growth) for the next three years.

Sensitivity to Changes in Social Security Provisions. Most legislative changes--including some already enacted and others now contemplated--affecting Social Security tax rates, benefit levels, and eligibility criteria automatically modify RRS Tier I

TABLE 4. ACTUAL AND PROJECTED FINANCIAL CONDITION OF RRS UNDER TWO ECONOMIC SCENARIOS: 1980-1990, DOLLARS IN BILLIONS

	1980	1982	1984	1986	1988	1990
	Based on CBO Assumptions					
Real Gross National Product (Annual growth in percents)	0.3	2.7	4.0	3.4	2.9	2.7
Railroad Employment (In thousands by calendar year) a/	531	495	493	494	489	484
RRS Income	4.35	5.62	6.48	7.17	7.86	8.80
RRS Outlays	4.76	5.68	6.39	7.03	7.68	8.26
Surplus or Deficit (-)	(0.41)	(0.06)	0.09	0.14	0.18	0.54
Accumulated Reserves at end of year	2.69	1.88	2.03	2.31	2.59	3.37
(As percent of outlays)	56.5	33.1	31.8	32.8	33.7	40.8
	Based on Data Resources, Inc. Assumptions					
Real Gross National Product (Annual growth in percents)	0.3	1.3	2.2	3.0	2.9	2.7
Railroad Employment (In thousands by calendar year) a/	531	491	477	468	462	457
RRS Income	4.35	5.62	6.51	7.15	7.74	8.51
RRS Outlays	4.76	5.68	6.40	7.03	7.65	8.21
Surplus or Deficit (-)	(0.41)	(0.06)	0.11	0.12	0.09	0.30
Accumulated Reserve, end of year	2.69	1.89	2.12	2.42	2.55	2.92
(As percent of outlays)	56.5	33.2	33.1	34.4	33.3	35.6

SOURCE: Data provided by the Railroad Retirement Board; computations based on CBO and Data Resources, Inc. economic assumptions of September 1981.

a/ Projections incorporate CBO estimates of employment reductions for CONRAIL and AMTRAK.

benefits. 4/ The notable exception to this linkage is the early-retirement annuity available to railroad workers with 30 or more years' service. Because of this exception, certain changes in Social Security provisions for early retirement (prior to age 65) would decrease the size of future transfer payments and would thus weaken the RRS's finances. For example, increasing the Social Security benefit reduction for persons retiring before age 65 would not affect annuities for new RRS retirees with more than 30 years of railroad service. But the reimbursement for these retirees' benefits from the Social Security transfer payment would reflect the new benefit reduction, and the RRS would have to finance a larger part of the Tier I benefit. Such changes in Social Security, however, would probably require a lengthy phase-in period and, if enacted, could be applied by the Congress to all RRS participants.

FEDERAL BUDGETARY COSTS

The costs of RRS--the only corporate pension program administered by the federal government--directly affect federal outlays and revenues. The impact on government receipts equals the difference between revenue received from RRS payroll tax collections and revenue forgone because railroad pensions are virtually exempt from federal income taxes. In addition, expenditures for RRS benefit payments and associated administrative expenses (regardless of financing sources) represent federal budgetary outlays. Put another way, the combined annual impact of railroad retirement on the federal budget represents a year's expenditures plus the loss of federal income taxes, less receipts from RRS payroll withholding taxes. 5/

The RRS's budgetary impact has increased from some $0.7 billion in 1970 to an estimated $2.6 billion in 1982 and is

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4/ The link of RRS withholding and taxable earnings rates to rises already legislated for Social Security will bring about one of the most predictable of these effects.

5/ Because RRS is a part of the federal budget, the transfer payments from Social Security, the interest paid by the U.S. Treasury, and the federal appropriations for windfall benefits represent internal budgetary transactions, not outlays.

projected to remain around $2.6 billion for each year between 1983 and 1987 (see Table 5). Within the present structure, the federal budgetary impact of RRS would be reduced by measures that increase RRS reserves--either through further payroll tax increases or through benefit limitations. Federal costs could also be reduced by withdrawing all or part of the tax-free status of RRS benefits. (The budgetary implications of changing the present federal role are discussed at the end of Chapter III.)

TABLE 5. PROJECTED IMPACT OF RRS ON THE FEDERAL BUDGET: 1983-1987, DOLLARS IN BILLIONS

	1983	1984	1985	1986	1987
Outlays (-)	-6.0	-6.4	-6.7	-7.0	-7.4
Revenues	3.4	3.7	4.0	4.4	4.8
Net negative budget impact	-2.6	-2.7	-2.7	-2.6	-2.6
Detail for Revenue Changes					
Revenue gained from RRS tax collections	3.8	4.0	4.4	4.8	5.2
Revenue forgone because of tax-exempt status of benefits a/ (-)	-0.4	-0.4	-0.4	-0.4	-0.4
Net revenue	3.4	3.7	4.0	4.4	4.8

SOURCE: Congressional Budget Office.

a/ These estimates represent the revenue impact of taxing all RRS benefits at rates consistent with the Economic Recovery Tax Act of 1981.

RRS COMPARED WITH OTHER PRIVATE-SECTOR RETIREMENT

Because RRS taxes already equal about 22 percent of the industry's payroll, any changes to safeguard further the future solvency of RRS would probably reduce benefits rather than increase payroll taxes. The Congress might also consider limiting RRS benefits in the context of government-wide budget reductions, even though the program now appears financially sound. For either reason, limitations on certain RRS provisions could help align the system more closely with other private-sector pension plans.

The rest of this chapter contrasts RRS with retirement practices in other parts of the private sector and concludes with an illustration of the so-called "disposable" portion of preretirement income replaced by RRS in comparison to that replaced by other retirement plans.

Benefit Differences

The RRS includes several benefit provisions that are more generous than most pensions in the private sector. Four features in particular account for the relative advantage of RRS over the pensions available to other private-sector workers:

- Early-retirement provisions,
- Spouse benefits,
- Annual cost-of-living adjustments, and
- Tax-exempt status.

In considering these RRS benefit advantages, however, one key counterpoint should not be overlooked: the 2 percent payroll tax railroad employees contribute toward Tier II benefits (discussed later in this chapter).

Age of Retirement. An RRS pension is available to a worker as early as age 60 and without any reduction in earned benefits for Tier I and Tier II so long as he has the equivalent of 30 years of railroad service. Prior to 1974, RRS benefits for all male retirees and for females with less than 30 years' service were reduced according to the Social Security formula.

The early-retirement provisions for career railroad employees contrasts sharply with those under Social Security (benefit reductions before age 65 and a minimum age of 62), which some critics regard as permitting retirement at too early an age. Because Social Security represents a large part of most retirees' income, few workers can afford earlier retirement even under plans that allow retirement before age 62. Most corporate pension plans--counterparts of RRS Tier II--only require a reduction in the earned annuity if retirement is elected before age 62 or, in some instances, age 55. 6/

In calculating length of railroad service, years of employment may either be consecutive or interrupted. This feature bridges changes from one company to another so long as all work is within the railroad industry. Such bridging over breaks in service and between firms is another superior feature.

More than 90 percent of the RRS employees retiring in 1980 were men, and more than half of them were younger than 62 years of age. On the other hand, male annuitants first receiving a Social Security retirement pension are, of course, much older--primarily because of age requirements and financial considerations. The striking difference in the ages at which retirees draw RRS and Social Security retirement benefits is illustrated by the following compilations of data for men 60 years of age and older: 7/

6/ About one-fourth of the 666 corporate pension plans surveyed by an independent actuarial firm permit retirement as early as age 62 without a reduction in earned benefits. See Hay-Huggins, Noncash Compensation Comparison, 1981, pp. V25-V27. A CBO review of eight selected plans in the transportation and utility industries found the larger plans not reducing benefits unless the retiree is under age 55.

7/ The RRS figures are calculated from data on males retiring under the system during 1980; retirees who were disabled or receiving deferred pensions are excluded. Social Security data cover men first awarded such benefits in 1977 (see Social Security Administration, Office of Research and Statistics, Annual Supplement 1977-1979, Table 65, p. 117). Data for both groups are the most recent available.

	Percent of New Enrollees	
Age at Retirement	Railroad Retirement	Social Security
60 and 61	57	None
62-63	21	41
64-65	18	51
66 and Over	4	8

Spouse Payments and Survivor Coverage. Unlike most corporate plans, the RRS includes a payment--generally equal to 45 percent of the Tier II benefit--to a nonworking spouse; this payment is in addition to the amount provided by the Social Security-type Tier I benefit. 8/ If the employee had at least 30 years of service, the payments may be received by the spouse at age 60 without any reduction. But if the railroad employee had less than 30 years of service, the spouse may not receive benefits until age 62 and such benefits are subject to the age reduction used by Social Security (1/144 for each month the spouse is younger than age 65). In addition, the RRS automatically provides for continuation of Tier II spouse benefits whenever the retired employee pre-deceases the spouse. This survivor coverage is a clear advantage over most private plans, which commonly extend such protection only if the employee elects a reduction in his corporate pension at retirement. (Like Social Security, RRS Tier I provides survivor coverage without a benefit reduction.)

Cost-of-Living Adjustments. Both portions of RRS pensions are automatically adjusted once a year for increases in the cost of living as measured by the Consumer Price Index (CPI). For Tier I, the cost-of-living adjustment (COLA) reflects the full CPI increase; for Tier II benefits, the COLA is calculated at just under one-third of the CPI increase.

8/ The spouse of a railroad retiree may resume work without losing either the Tier I or Tier II spouse payment if employment is neither with the railroad industry nor with anyone who employed the spouse just before the spouse payment was first received. The Tier I spouse payment is reduced, however, if the spouse receives Social Security benefits.

The limit on the size of the Tier II COLAs appears consistent with recent experience of private-pension retirees, but the RRS guarantee of an automatic adjustment each year is superior. Relatively few (4 to 8 percent) private-sector pension plans have an explicit COLA provision, and approximately 40 percent grant no COLA of any kind. Most private companies' plans adjust benefits on an unscheduled, ad hoc basis. 9/

Exemption From Federal Taxation. Virtually all RRS benefits are tax free. 10/ This provides a pecuniary advantage for RRS annuitants, because only the Social Security portion of retirement income received by other private-sector annuitants is tax free. For example, in calendar year 1983, married railroad annuitants--with RRS pension benefits ranging between $20,000 and $22,000--will receive an annual federal income tax advantage averaging some $1,200 per couple. After a railroad annuitant and his spouse both reach age 65, the tax advantage on the same income shrinks to about $900 because of the extra tax exemptions available to older persons. 11/ Because of graduated federal income tax rates, the advantage of a tax-free RRS pension increases to the extent that a railroad annuitant has taxable income from other sources.

Employee Contributions. Because of Tier II taxes, railroad employees pay some 2.0 percent of covered payroll more toward their retirement than do most other private-sector workers covered by Social Security and a corporate pension plan. In January 1982, railroad employees will pay a 5.4 percent tax on earnings up to $32,400 per year for Tier I benefits (excluding health-care

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9/ Appendix B summarizes recent surveys that have collected data on COLAs available to private-sector retirees.

10/ The longevity supplement is the only RRS benefit subject to federal income taxation, but because of the small size of this benefit, no taxes would be collected unless the average annuitant under age 65 reported taxable income exceeding $3,300 if single and $5,400 if married and filing a joint return.

11/ The estimates reflect implementation of the tax reductions the Congress enacted in 1981. In addition, the hypothetical employee considered here is assumed to retire at age 62 with 36 years of service.

coverage) and an additional 2.0 percent tax on earnings up to $24,300 per year for Tier II benefits. 12/ Because most corporate plans are fully paid by the employer, most employees in the private sector pay only the equivalent of the 5.4 percent Tier I/Social Security tax.

Wage Replacement

Taken together, the RRS provisions offer attractive income security at relatively early ages for employees who spend all or most of their careers with the railroad and who have nonworking spouses. For these people, accounting for more than half of those retiring directly from the railroad each year, RRS provides a retirement package that seemingly ranks among the highest in private industry.

This conclusion is supported by comparing the replacement of wages--just before retirement and after taxes--under RRS and under other private-sector retirement plans. The private-sector retirement examples combine Social Security with either a hypothetical company plan (a composite constructed by CBO) for blue-collar workers in all industries, or with selected plans in the transportation service and utility industries (see Table 6). 13/ The RRS replacement rates for married annuitants exceed the highest of the selected other plans reviewed in the transportation service and utilities industries. The rate of disposable income replacement for single RRS annuitants appears close to average private-sector practice.

12/ Estimated average earnings per railroad job will increase from $27,400 in 1981 to about $29,600 in 1982.

13/ For a detailed description of the composite plan see CBO *Alternative Approaches to Adjusting Compensation for Federal Blue-Collar Employees* (November 1980), pp. 38-40. The selected plan descriptions (covering 1.7 million employees in the utilities and transportation service industries) include two provided by the Bureau of Labor Statistics and six provided by the Bankers Trust Company in *Corporate Pension Plan Study* (1980), pp. 242-263.

TABLE 6: EXAMPLES OF WAGE REPLACEMENT RATES UNDER RRS AND OTHER PRIVATE SECTOR RETIREMENT: WAGE REPLACEMENT AS A PERCENT OF FINAL SALARY AFTER TAXES

	Final Gross Salary	
	$22,000	$30,000
	(For Married Retirees a/)	
Railroad Industry	129	105
All Industries b/	97	76
Select Transportation and Utility Company Plans c/	104	89
High benefits	(118)	(99)
Low benefits	(92)	(73)
	(For Single Retirees)	
Railroad Industry	96	79
All Industries b/	83	66
Selected Transportation and Utility Company Plans c/	90	80
High benefits	(105)	(90)
Low benefits	(77)	(63)

SOURCE: Congressional Budget Office.

NOTE: Workers assumed to retire at age 62 after 36 years of service. See Chapter I, footnote 8.

a/ Spouse assumed to be age 62 to reflect Social Security spouse benefits.

b/ Combines Social Security and composite company benefits for blue-collar workers. See CBO, Alternative Approaches to Adjusting Compensation, pp. 38-40.

c/ Estimates represent the average retirement benefits covering a population of 1.7 million transportation and utility workers in eight selected plans. The sources for the selected plans are described in footnote 13 on the preceeding page.

CHAPTER III. ALTERNATIVE BENEFIT PROVISIONS

In considering what if any action to take with regard to RRS, the Congress will want to weigh several factors. Modifications in the system could be designed to align it more closely with other private-sector retirement practices, to lower federal budgetary costs, or to fortify further the program's financial condition. As Chapter II states, however, it is unlikely that the Congress will need to consider benefit reductions solely as a safeguard against future financial crisis for RRS or as contingency measures that could be invoked later. 1/ Alternatively, the Congress may want to assess a more radical course that would limit the federal role in RRS (discussed at the end of this chapter).

In order to illustrate the maximum impact of various possible modifications to the current RRS, two alternatives discussed in this chapter go beyond aligning railroad retirement with practices of other private-sector employers. The Congress could blend or scale these measures to fit particular requirements for RRS or the federal budget. Or as is always the case, the Congress could decide that the best course would be a continuation of the present system (Option I). Three possible changes, all dealing with RRS benefits because withholding rates were increased significantly in 1981, are examined below:

- Reducing benefits for early retirement (Option II);
- Reducing Tier II benefits for spouses (Option III); and
- Taxing benefits (Option IV).

1/ As noted in Chapter I, the President must send the Congress a report, within a year, on RRS financial condition along with recommendations for any needed long-term changes in benefits or funding. In addition, the Railroad Retirement Board is required to notify Congress by April 1 in any year that projections show half of the newly authorized borrowing authority will be depleted and, if necessary, to reduce benefits in a fair and equitable manner. The Board's actions must assure that each recipient's benefits would at least equal what would otherwise be received if railroad service had been covered by Social Security.

The cumulative five-year reductions generated by the three alternatives range from $0.1 billion under Option III to $1.9 billion under Option IV (see Table 7 later in this chapter). The savings would reduce the federal budget and at the same time, could increase the buildup of RRS reserves. (For estimating purposes, the assumed effective date of each option is October 1982. As a practical matter, the effective dates could differ as could scope, duration, and timing of particular measures.)

OPTION I. CONTINUE THE CURRENT SYSTEM

According to projections prepared for CBO by the Railroad Retirement Board, RRS reserves will continue to grow throughout the next five years, increasing from $1.9 billion at the end of 1983 to $2.4 billion in 1987. During this same period, the system's annual impact on the federal budget is projected to remain around $2.6 billion--a 25 percent greater burden on the budget than if, hypothetically, present benefits and employee withholdings were aligned with other private-sector retirement practices.

Opponents of the present system oppose it as too costly to the industry (the effective 22 percent payroll tax) and overgenerous to retirees, especially younger ones. In their view, it would be prudent to reduce RRS payroll taxes by scaling back the current benefit structure. Alternatively, certain particular benefit cutbacks could bring the RRS into closer alignment with other private-sector retirement, thus providing a larger cushion in RRS reserves and smaller federal budgetary costs.

Advocates of the current RRS program point out that the Congress just modified the system--expressing a degree of Congressional commitment--and believe that these changes assure adequate finances for the future. Even though certain benefits features are more liberal than those in other plans, they are mostly paid for by railroad companies and workers. Some would argue that any adverse impact the RRS may have on the federal budget represents a short-term accounting problem, not a permanent burden on taxpayers. A counter to this view is that it overlooks annual federal appropriations to the RRS and the federal tax exemption enjoyed by railroad annuitants.

OPTION II. REDUCE BENEFITS FOR EARLY RETIREMENT

Option II would reduce both primary and spouse RRS benefits currently available to retirees with 30 or more years of service. The initial annuity reductions would reflect the early retirement factors used by Social Security. This change would be a reversion to the pre-1974 RRS provisions, and it would be stricter than provisions generally found elsewhere in the private sector (see discussion in Chapter II).

For employees retiring at age 60 with at least 30 years railroad service, the Option II reduction would decrease earned benefits by one-third (60 months times 1/180). For a hypothetical married employee with a final salary of $30,000, RRS benefits would fall from 105 percent to 87 percent of net final salary before retirement and after taxes. (The calculations assume that the annuitant retires at age 62 after 36 years of rail service, and that RRS income remains tax exempt.)

Reinstatement of the monthly reduction, disregarding length of service, for all new RRS retirees would delay retirement or reduce benefits for approximately 10,000 persons per year. This would lighten the annual cost burden for RRS by about $110 million in the first year and $160 million four years later. An early-retirement reduction proposal, such as Option II, would probably require authorizing legislation that incorporates certain retroactive provisions. Otherwise, retirement rates and associated RRS costs would rise sharply as employees accelerated retirement plans to avoid impending benefit reductions.

In light of current proposals to increase early-retirement reductions for Social Security, some observers might view Option II as not going far enough. Others would critize the option because many railroad workers have undoubtedly already made plans to retire early 2/; questions would surely arise as to why present annuitants were spared any financial sacrifice. It should be noted, however, that in some cases early-retirement annuities available under Option II would continue to exceed after-tax income received just before retirement.

2/ Some 118,400 railroad employees have the equivalent of 29 or more years of service; 14 percent are age 62 or older, 15 percent are age 60 or 61, 35 percent are between age 55 and 60; and the remaining 36 percent are age 55 or younger.

OPTION III. REDUCE TIER II SPOUSE BENEFITS

Option III would bring RRS Tier II spouse payments into closer alignment with retirement practices in the rest of the private sector. Two changes would result: first, Tier II spouse payments would no longer be adjusted for increases in the cost-of-living; and second, the new plan would eliminate the automatic payment of Tier II survivor benefits for spouses of current and future retirees. The Tier II survivor protection (based on current benefit provisions) would continue only if a railroad retiree elected a modest reduction in his Tier II benefit. Taken together, the changes in Option III would reduce costs by some $120 million through 1987. (The option would not affect either present annuities for current survivors or prospective survivor payments to spouses of employees who die prior to retirement.)

According to information collected by the Bureau of Labor Statistics and by the actuarial firm of Hay Associates, company pensions do not include any payment for the spouses of living retirees. In most cases in which spouse survivor protection is available, the employee must have accepted an actuarial reduction in his initial annuity or waived coverage. An annuity reduction for elective survivor protection could, of course, be more modest than one based on actuarial factors. For example, federal retirees who elect to provide survivor protection to their wives or husbands have their initial annuities reduced by 2.5 percent of the first $3,600 of annual income, plus 10 percent of income over $3,600. Applying this formula to the RRS would reduce cumulative Tier II outlays by $80 million between 1983 and 1987.

Suspending the annual cost-of-living adjustments in Tier II spouse benefits would avoid reductions both in the initial annuity awarded new beneficiaries and in present spouse payments. It also would recognize the unique benefit advantage available to married railroad retirees, which, for obvious reasons, seems inequitable to some annuitants and taxpayers.

Proponents of Option III point out that, even with the proposed reductions in spouse payments, initial RRS benefits for married annuitants would still exceed their railroad wages just before retirement and after taxes. Opponents counter that the RRS spouse and survivor benefits were recently changed by the Congress (see Appendix B), and that further revisions would breach standing agreements between labor and management. The opposition would also point out that the reductions would affect the prospective survivor benefits of a group that would be hard pressed by an income cut. Single and widowed employee annuitants could argue, however, that a person's marital status should not influence the size of a corporate pension. From their perspective, Option III should further limit spouse benefits as a means to increase the railroad employee's annuity.

OPTION IV: TAX RAILROAD RETIREMENT BENEFITS

Option IV would withdraw the tax-free status of RRS benefits. This alternative, requiring amendment to the original RRS provisions of 1935, would reduce federal costs for RRS in the form of income tax receipts forgone under current law. The federal budgetary savings would begin at some $360 million in the first year and accumulate to about $1.9 billion over five years.

If, as an accompanying contingency measure, it were decided to augment RRS reserves, Option IV could be modified by authorizing new federal appropriations corresponding to the estimated increase in federal tax revenues. This approach would not increase costs to the federal government but would replace the indirect tax subsidies (revenues forgone) with additional direct appropriations. (The current federal appropriations to RRS for windfall benefits would not be affected by this modification.)

Discontinuing the RRS tax advantage would help federal budget-cutting efforts, but at an expense to railroad annuitants. For example, the portion of income (before retirement and after taxes) retained by a hypothetical retiree would decline from 105 percent to 96 percent under Option IV. 3/ But this approach would allocate the financial sacrifice among railroad annuitants according to their total taxable income. Individuals best able to accommodate the reduction would likely bear the greatest burden, and low-income annuitants would face little if any additional tax burden.

Option IV would represent a departure from typical private-sector practice inasmuch as Social Security income is exempt from federal taxation. If requirements to reduce the federal budget

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3/ The calculations assume that a new railroad retiree is married, has 36 years of rail service, retires at age 62 with a gross salary of $30,000, and is eligible for windfall benefits.

TABLE 7: ESTIMATED ANNUAL SAVINGS FROM RRS MODIFICATIONS: DOLLARS IN BILLIONS

	In First Year	In Fifth Year	Cumulative Five-Year Savings
Option I: Current System	--	--	--
Option II: Reduce Benefits for Early Retirement	0.11	0.16	0.71
Option III: Reduce Tier II Spouse Benefits	0.02	0.03	0.12
Option IV: Tax Railroad Retirement Benefits	0.36	0.41	1.90

SOURCE: Congressional Budget Office.

NOTE: For estimating purposes, options are assumed to take effect October 1, 1982.

called for a less far-reaching action, the Congress could continue the tax exclusion for half of RRS retirement income; this would approximate the Social Security tax exclusion. Such a more limited exemption might be viewed as sound public policy regardless of RRS financial considerations, but it would yield smaller savings--accumulating to some $0.9 billion in the first five years.

CHANGING THE FEDERAL ROLE--A BASIC DEPARTURE

Under each of the above alternatives for modifying RRS, programmatic and financial responsibility for railroad retirement would remain with the federal government. 4/ Some analysts have

4/ The Railroad Retirement Board administers RRS with a 1,580 federal workforce and an operating budget of some $60 million.

argued for a fundamental departure from this arrangement. For example, the current federal involvement could be scaled back by taking the corporate-type portion (RRS Tier II benefits) out of the federal budget. Proponents of such an approach believe that it would improve the financial accountability of the RRS, because rail management and labor would be directly responsible for the formulation and implementation of future financing or benefit changes.

Collective bargaining for RRS corporate-type benefits would be more consistent with labor-management relations in other industries. Such an approach would relieve the federal government of its existing statutory responsibility for these benefits. In principle, this represents an extension of provisions contained in the 1981 amendments that call for industry and labor to develop recommendations whenever the need for changes in the RRS becomes apparent. As a practical matter, however, changes in the federal government's present involvement could encounter several budgetary and administrative problems, including the prospect of duplicative organizations to administer separate RRS benefit components.

Although restructuring the RRS to reduce the role of the federal government could take many forms, the basic ingredient would be the off-budget administration of Tier II benefits. Because Tier II tax revenues, under current law, are projected to exceed benefit demands, the federal budget will enjoy a net gain. If the Tier II program were moved off budget, however, this advantage would disappear--the resulting net annual loss to the government would grow from $0.1 billion in 1983 to some $0.4 billion in 1987. In addition, large one-time increases in federal outlays could result from certain potential transition requirements concerning liquidation of the $1.9 billion held in RRS reserves and final reimbursement for some $3.6 billion in Social Security-type benefits already paid by RRS.

Several features might be designed to moderate or defer such effects, but they would be accompanied by continued federal involvement. To change the present RRS structure, the government would also need to address other complex decisions regarding funding for windfall benefits and whether provisions of the Employment Retirement Income Security Act (ERISA) should cover the new railroad program.

APPENDIX A. SUMMARY OF CHANGES IN RAILROAD RETIREMENT BENEFITS CONTAINED IN THE OMNIBUS BUDGET RECONCILIATION ACT OF 1981

Prior Law	Current Law as Amended
Calculations of Employee Tier II Benefits	
The calculation of employee Tier II annuities included three parts: a component for service prior to 1974; a component for post-1974 service, and a component for employees who worked both before and after 1974.	For new retirees, employee Tier II annuities calculated as 0.7 percent of the employee's average monthly compensation for the 60 highest months of earnings times each year of service. The amount is then reduced by 25 percent of any monthly amount received from RRS windfall/dual benefits.
Employee Tier II Cost-of-Living Adjustment	
Statutory authority for COLAs, tied to 32.5 percent of annual Social Security adjustments, expired in 1981.	Permanently continues annual Tier II COLAs.
Eligibility for Tier I Spouse and Survivor Benefits	
Divorced wives of railroad employees were not eligible for RRS payments.	Provides Tier I spouse payments for a divorced wife who is at least age 62, had been married to the employee for at least 10 years, and is currently unmarried. This change conforms RRS to Social Security.
Tier I survivor benefits were not available to divorced wives, remarried widows, and divorced mothers.	Provides Tier I survivor benefits to divorced wives, remarried widows, and divorced mothers so long as such persons would have qualified for Social Security benefits if the railroad service of the deceased employee or annuitant had been covered by Social Security. This change conforms RRS to Social Security.

(continued)

Prior Law	Current Law as Amended
Calculations of Tier I and II Spouse Payments	
The spouse's Tier II payment equaled 50 percent of the retired employee's Tier II annuity up to a maximum amount.	The spouse's Tier II payment for new awards equals 45 percent of the retiree's Tier II annuity without limit.
For employees with less than 30 years of service, the initial spouse payment was reduced by 1/180 per month before the spouse's 65th birthday.	Increases the reduction to 1/144 per month under age 65.
Calculation of Tier II Survivor Benefits	
A surviving widow or widower's Tier II benefit equaled 30 percent of the deceased employee's Tier I benefit. The survivor benefit was indexed at 100 percent of annual Social Security adjustments.	A surviving spouse's Tier II benefit equals 50 percent of the deceased employee's Tier II benefit. The change in survivor benefits is not effective until October 1, 1986 except for survivors of employees dying after October 1, 1981. Indexation for all survivors is immediately reduced to 32.5 percent of annual Social Security COLA.
Eligibility for Longevity Supplement	
Longevity supplements were available for annuitants who retire directly from the railroads with at least 25 years of service.	Employees first hired after October 1, 1981 are not eligible for longevity supplements, regardless of length of rail service.

(continued)

Prior Law	Current Law as Amended
Windfall/Dual Benefit	
Appropriations and outlays for windfall/dual benefits were paid out of the general Railroad Retirement account.	Creates a separate account for dual/windfall payments. If appropriated amounts are not adequate to cover estimated costs, windfall benefits are reduced accordingly.
The calculation of benefits recognized changes in the cost of living from 1974 to the date of retirement.	Discontinues further pre-retirement indexing of windfall benefits. Also applies the age reduction factor to all parts of the formula for calculating windfall benefits.
In determining eligibility for windfall benefits, married women were allowed to include their spouses' employment covered by Social Security. The courts had ruled that this provision should also be available to married male railroad retirees.	Eliminates spouse's employment under Social Secuity as a factor determining windfall benefit eligibility for both men and women. Also, eliminates future windfall awards to spouses and survivors.

Other Amendments

Credit is allowed for actual months of service instead of rounding to the next full year for six or more months of service.

Technical changes are made in calculating Tier I and Tier II cost-of-living adjustments for employees who retired before age 65 with less than 30 years of service.

APPENDIX B. INFORMATION ON COST-OF-LIVING ADJUSTMENTS IN THE PRIVATE SECTOR

Recent surveys have collected data on COLAs in private-sector pensions. Summaries of these surveys follow.

Bankers Trust Corporate Pension Plan Study 1980, Section 2, pp. 52-55.

The Bankers Trust Study of 325 pension plans covering more than 8 million employees found that only 4 percent (13 plans) provided cost-of-living adjustments based on changes in the Consumer Price Index. In nine of these plans, annual changes were made automatically, but increases were limited to 4 percent per year. Another 32 percent made pension adjustments, mostly unscheduled, on some basis other than changes in CPI.

For the plans that granted post-retirement increases of any kind during the six-year period 1975-1980, none granted increases every year: 45 percent of the plans gave one increase, 35 percent gave 2 increases, 5 percent gave 3 increases, 5 percent gave 4 increases, and 10 percent gave 5 increases.

Hay-Huggins Noncash Compensation Comparison, 1981, Section V, pp. V18-V21.

The spring 1981 survey of 666 corporate retirement plans, covering some 5.7 million participants, found that 42 percent (280 plans) do not grant COLAs and that only 8 percent (53 plans) have formal COLA provisions, but most with a limit on the size of the adjustment--ranging from 2 percent to 5 percent. The remaining 50 percent (333 plans) provide COLAs on an ad hoc basis. Of these, only 12 percent (41 plans) provided an adjustment in 1981; 35 percent (115 plans) provided the last COLA in 1980; and 53 percent (177 plans) provided the last COLA in 1979 or before.

Towers, Perrin, Foster and Crosby Analysis

From January 1, 1975 through December 31, 1979, annual COLA increases for 100 private-sector pension plans averaged one-third of the change in the CPI. Specifically, the average annual increase (weighted for plan size) was 2.7 percent, compared to an annual inflation rate of 8.1 percent. The TPF & C study, conducted for the U.S. Office of Personnel Management, analyzed the magnitude of COLAs for 100 private pension plans that covered over 2 million employees; frequency of adjustments was not identified.

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